

Prepare debenture account, debenture redemption fund account and debenture redemption fund investment account. (5 marks)

Answer 1(a)(i)**Incorrect**

Accounting Standards (AS) are formulated by Accounting Standards Board which has been constituted by Council of the Institute of Chartered Accountants of India. The Central Government, in consultation with the National Advisory Committee on Accounting Standards, issues Accounting Standards under Companies (Accounting Standards) Rules, 2006.

Answer 1(a)(ii)**Incorrect**

Through the introduction of Section 77A in the Companies Act, 1956 by the Companies (Amendment) Act, 1999, the Central Government has allowed the buy-back of its own shares by the companies. The shares can be purchased subject to satisfaction of conditions as provided under Section 77A(2).

Answer 1(a)(iii)**Correct**

Under the Companies (Transfer of Profit to Reserves) Rules, 1975 as amended, if the rate of dividend is more than 20%, then 10% of profits is to be transferred to reserve.

Answer 1(a)(iv)**Incorrect**

The law (Companies Act, 1956) limits the commission in case of issue of shares to 5% of the issue price of shares and in case of debentures to 2.5% or such lower rate as is provided in the Articles of Association.

Answer 1(a)(v)**Incorrect**

Contingent liabilities relating to outsiders are not shown on the liability side of the consolidated balance sheet. It will be shown as contingent liability by way of note/ footnote.

Answer 1(b)

- (i) According to the provisions of Section 198 of the Companies Act, maximum limit on the total managerial remuneration payable by public company is **11%** of net profits.
- (ii) A company must pay the dividends within **30 days** of its declaration.
- (iii) Preliminary expense is a **fictitious** asset.
- (iv) Discount on the issue of debenture is a **capital** loss.
- (v) If the purchase price of the debenture includes the interest for the expired period, it is known as **cum-interest purchase/quotation**.

Answer 1(c)

<i>Dr.</i>			12% Debentures Account			<i>Cr.</i>		
<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>	<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>			
31.3.09	To Debentureholders	1,70,000	1.4.08	By Balance b/d	10,00,000			
	To Profit on Redemption of Debentures A/c	30,000						
	To Balance c/d	8,00,000						
		10,00,000						10,00,000
			1.4.09	By Balance b/d	8,00,000			

Debenture Redemption Fund Account

<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>	<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>
31.3.09	To Capital Reserve (Rs.30,000 + 7,000)	37,000	1.4.08	By Balance b/d	4,50,000
	To General Reserve	1,80,000	31.3.09	By P&L Appropriation A/c	90,000
	To Balance c/d	3,90,000		By Interest on Debenture Redemption Fund Investment (DRFI) A/c (6% of 5,00,000)	30,000
				By DRFI A/c (profit on sale of investment)	7,000
				By Profit on Redemption of Debentures	30,000
		6,07,000			6,07,000

Debenture Redemption Fund Investment Account

<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>	<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>
1.4.08	To Balance b/d	4,50,000	31.3.09	By Bank	1,87,000
31.3.09	To Bank	1,20,000		By Balance c/d	3,90,000
	To DR Fund A/c (profit on sale)	7,000			
		5,77,000			5,77,000

Note : It is assumed that Rs. 20,000 of debentures have been redeemed out of capital and therefore debentures with face value of Rs. 1,80,000 has been redeemed out of Debenture Redemption Fund Account.

Question 2

(a) Write short notes on any two of the following :

(i) Accounting Standard-10 : Accounting for fixed assets

(ii) Issue of shares at a discount

(iii) Taxation on distributed profits. (3 marks each)

(b) Following are the abridged balance sheets of Hary Ltd. and Say Ltd. as on 31st March, 2009 :

Liabilities	Hary Ltd. (Rs.)	Say Ltd. (Rs.)
Equity share capital (Rs. 100 each)	10,00,000	5,00,000
General reserve	1,00,000	1,70,000
Profit and loss account	1,60,000	1,30,000
Current liabilities	4,40,000	2,00,000
	<u>17,00,000</u>	<u>10,00,000</u>
Assets		
Fixed assets	4,80,000	2,50,000
Investment in shares of Say Ltd.	5,00,000	—
Current assets	7,20,000	7,50,000
	<u>17,00,000</u>	<u>10,00,000</u>

Additional information :

(i) On 1st July, 2008, Hary Ltd. acquired 3,000 shares in Say Ltd. The reserves and surplus position of Say Ltd. as on 1st April, 2008 was as under :

General reserve Rs. 2,50,000

Profit and loss a/c (Cr.) Rs. 1,20,000

(ii) On 1st October, 2008, Say Ltd. issued one equity share for every four shares held as bonus shares out of general reserve. No entry has been made in the books of Say Ltd. for issue of bonus shares.

(iii) On 30th September, 2008, Say Ltd. declared a dividend out of pre-acquisition profits @ 25% on Rs.4,00,000, its capital on that date. Hary Ltd. credited the dividend to its profit and loss account.

(iv) Say Ltd. owed Hary Ltd. Rs.50,000 for purchase of stock from Hary Ltd. The entire stock is held by Say Ltd. on 31st March, 2009. Hary Ltd. made a profit of 25% on cost.

Prepare a consolidated balance sheet of Hary Ltd. and its subsidiary Say Ltd. as on 31st March, 2009. (9 marks)

Answer 2(a)(i)**AS-10 - Accounting for Fixed Assets**

Financial statements disclose information regarding fixed assets such as land and building, plant and machinery, vehicles, furniture and fittings, goodwill, patents, trade marks and designs, etc. The cost of fixed asset should comprise its purchase price and any attributable cost of bringing the asset to its working condition for its intended use. In case of self constructed assets, only direct costs are included in the cost of the asset. In an exchange of assets, the cost of assets given up should be taken as the value of new asset. Fixed asset should be eliminated from the financial statements on disposal or when no further benefit is expected from its use. Losses arising from the retirement or gains or losses arising from disposal of fixed asset which is carried at cost should be recognized in the profit and loss account.

When fixed assets are revalued, an entire class of assets should be revalued or the selection of assets for revaluation should be made on systematic basis. When a fixed asset is revalued upwards, accumulated depreciation existing at the date of revaluation should not be credited to profit and loss account. An increase in net book value arising on revaluation of fixed assets should be credited directly to owner's interest under revaluation reserve. Fixed assets acquired on hire-purchase should be disclosed only at net cash value stating the fact of hire purchase. Where several fixed assets are purchased for a consolidated price, the consideration should be apportioned to various assets on a fair basis as determined by competent valuers. Goodwill should be recorded only when some consideration in money has been paid for it.

The following information should be disclosed in the financial statements :

- (i) Gross and net book values of fixed assets at the beginning and at the end of the accounting period-showing additions, disposals, acquisition etc.
- (ii) Proper disclosure should also be made regarding expenditure incurred in the course of construction or acquisition.
- (iii) Information in respect of revalued assets should include revalued amount substituted for historical cost of fixed assets, the method adopted to compute the revalued amounts, the nature of indices used, the year of any appraisal made and whether an external valuer was involved, etc.

Answer 2(a)(ii)**Issue of Shares at Discount**

When shares are issued at a price lower than the face value, they are said to be issued at discount. Section 79 of the Companies Act, allows a company to issue shares at a discount subject to the following conditions:

- (i) The shares must belong to a class already issued.
- (ii) The issue is authorised by a resolution passed in the general meeting of the company and the sanction of the Central Government is obtained.
- (iii) The resolution must specify the maximum rate of discount at which the shares

are to be issued. No resolution shall be sanctioned by the Central Government if the maximum rate of discount specified in the resolution exceeds ten per cent, unless it is of opinion that a higher percentage of discount may be allowed in special circumstances of the case.

- (iv) Not less than one year has at the date of the issue elapsed since the date on which the company was entitled to commence business.
- (v) The shares must be issued within two months from the date of receiving the sanctions of the Central Government or within such extended time as the Central Government may allow.

The discount on issue of shares must be treated as a loss of capital nature and debited to a separate account called 'Discount on Issue of Shares Account'. Until it is written off, it must be shown on the assets side of the Balance Sheet under the head "Miscellaneous Expenditure". It is written off gradually out of profits over a reasonable number of years.

Answer 2(a)(iii)

Taxation on Distributed Profits

The Finance Act, 1997 introduced, an additional income tax, known as tax on distributed profits, on joint stock companies. This tax is designated as tax on distributed profit or dividend distribution tax or corporate dividend tax. Section 115O(1) of the Income-tax Act lays down that any amount declared, distributed or paid by a domestic company by way of dividend, whether interim or otherwise shall be charged tax on distributed profits at specified rates. It is paid in addition to the income tax chargeable on total income. The dividend chargeable to tax on distributed profit may be out of current profits or accumulated profits. The tax on dividend shall be payable even if the company has to pay no tax on profits. Further, it is specified that the tax has to be paid within 14 days from the date of : (a) declaration of dividend, (b) distribution of dividend, or (c) payment of dividend, whichever is earliest. Like rates of income tax, the rate of tax on distributed tax may vary from one financial year to other year.

As tax on distributed profit is levied on the profits distributed, it should be shown below the line i.e. in profit and loss appropriation account. In case of interim dividend, the tax will normally be paid in the same accounting year in which the dividend is declared and paid. In case of proposed dividend, a provision for tax on distributed profit on the amount proposed to be distributed should be made and shown along with the proposed dividend in the profit and loss appropriation account. Thus, tax on distributed profit liability should be disclosed in the profit and loss appropriation account as under:

To Proposed Dividend	XXX
To Tax on Distributed Profit	XXX

In the balance sheet, tax on distributed profit should be shown separately under the head 'Provisions'.

Answer 2(b)

**Consolidated Balance Sheet of Hary Ltd. and its Subsidiary Say Ltd.
on 31.3. 2009**

<i>Liabilities</i>	<i>Rs.</i>	<i>Assets</i>	<i>Rs</i>
<i>Share Capital</i>			
Equity Share Capital (Rs.10 each)	10,00,000	<i>Fixed Assets :</i>	
Minority Interest	2,00,000	Hary Ltd.	4,80,000
<i>Reserves & Surplus :</i>		S Ltd.	<u>2,50,000</u>
Capital Reserve	1,01,875	<i>Current Assets:</i>	
General Reserve	1,00,000	Hary Ltd.	7,20,000
Profit & Loss Account :		Say Ltd.	<u>7,50,000</u>
Hary Ltd.	1,60,000		<u>14,70,000</u>
<i>Less : Dividend wrongly</i>			
credited	75,000	<i>Less : Mutual Owings</i>	<u>50,000</u>
	<u>85,000</u>		<u>14,20,000</u>
<i>Add : H. Ltd's Share in</i>			
Revenue profit of Say Ltd	73,125	<i>Less : Unrealised Profit</i>	<u>10,000</u>
	<u>1,58,125</u>		14,10,000
<i>Less : Unrealised Profit</i>	10,000		
<i>Current Liabilities :</i>			
Hary Ltd.	4,40,000		
Say Ltd.	<u>2,00,000</u>		
	6,40,000		
<i>Less : Mutual Owing</i>	50,000		
	<u>5,90,000</u>		
	<u>21,40,000</u>		<u>21,40,000</u>

Working Notes :**(i) Capital Profits (Pre-acquisition profits)**

	<i>Rs.</i>	<i>Rs.</i>
General Reserve (1.4.2008)	2,50,000	
<i>Less : Bonus issue</i>	<u>1,00,000</u>	
Pre-acquisition Reserve		1,50,000
Profit & Loss A/c (1.4.2008)	1,20,000	
<i>Less : Dividend out of pre-acquisitions profit</i>		
(25% on Rs.4,00,000)	<u>1,00,000</u>	20,000
Profit of Current Year (pre-acquisition)		
(1.4.2008 to 30.6.2008)		<u>32,500</u>
		<u>2,02,500</u>
Hary Ltd.'s share (75%)		1,51,875
Minority Interest		<u>50,625</u>

(ii) Revenue Profits (1.7.2008 to 31.3.2009)

Rs.

Profit & Loss A/c as on 31.3.2009	1,30,000
Less : Opening Balance (1,20,000 – 1,00,000)	20,000
	<u>1,10,000</u>
Add : Transfer to Reserve (Rs.1,70,000 – 1,50,000)	20,000
Profits earned during the year	<u>1,30,000</u>
Profit for the pre-acquisition period (Rs.1,30,000 x 3/12)	32,500
Profit for the post-acquisition period (Rs.1,30,000 x 9/12)	<u>97,500</u>
Hary Ltd. Share (3/4)	73,125
Minority Interest	<u>24,375</u>

(iii) Calculation of Capital Reserve

Rs.

Paid up capital	3,00,000
Share of bonus shares	75,000
Share of capital profit	<u>1,51,875</u>
	<u>5,26,875</u>
Less : Cost of Investment	5,00,000
Less : Dividend out of capital profit credited to Profit & Loss Account	<u>75,000</u>
Capital Reserve	<u>1,01,875</u>

(iv) Minority Interest

Share Capital	1,00,000
Share of bonus shares	25,000
Share of capital profits	50,625
Share of revenue profits	<u>24,375</u>
	<u>2,00,000</u>

Question 3

(a) Abridged balance sheet of Rama Ltd. as on 31st March, 2009 is as follows :

<i>Liabilities</i>	<i>Rs.</i>
<i>Share capital</i>	<i>6,00,000</i>
<i>Reserves and surplus</i>	<i>50,000</i>
<i>Bank overdraft</i>	<i>10,000</i>
<i>Creditors</i>	<i>60,000</i>
<i>Provision for taxation</i>	<i>1,10,000</i>
<i>Proposed dividend</i>	<i>60,000</i>
	<u><u>8,90,000</u></u>

Assets

<i>Fixed assets</i>	<i>3,70,000</i>
<i>Current assets</i>	<i>5,20,000</i>
	<u><i>8,90,000</i></u>

The net profits of the company after deducting working expenses but before providing for taxation were as under :

<i>Year</i>	<i>Rs.</i>
<i>2006-07</i>	<i>3,18,000</i>
<i>2007-08</i>	<i>3,40,000</i>
<i>2008-09</i>	<i>3,12,000</i>

On 31st March, 2009, fixed assets were at Rs.4,50,000. Sundry debtors on the same date included Rs.10,000 which is irrecoverable. Having regard to the type of business, a 10% return on average capital employed is considered as reasonable. Ascertain the value of goodwill on the basis of three years purchase of annual super profits. Also calculate goodwill by capitalisation of average maintainable profits. Depreciation on fixed assets is charged @ 10% per annum and the rate of tax is 30%. (6 marks)

- (b) *Following is the profit and loss account of Azad Ltd. for the year ended 31st March, 2009 :*

	<i>Rs.</i>
<i>To Office and administrative expenses</i>	<i>3,10,000</i>
<i>To Selling and distribution expenses</i>	<i>1,92,000</i>
<i>To Directors' fees</i>	<i>39,500</i>
<i>To Managerial remuneration</i>	<i>1,70,000</i>
<i>To Interest on debentures</i>	<i>18,500</i>
<i>To Donation to charitable trust</i>	<i>15,000</i>
<i>To Compensation for breach of contract</i>	<i>27,000</i>
<i>To Depreciation on fixed assets</i>	<i>3,12,000</i>
<i>To Investment revaluation reserve</i>	<i>12,500</i>
<i>To Provision for taxation</i>	<i>7,40,000</i>
<i>To General reserve</i>	<i>2,50,000</i>
<i>To Balance c/d</i>	<i>8,46,500</i>
	<u><i>29,33,000</i></u>
<i>By Balance b/d</i>	<i>3,43,200</i>
<i>By Gross profit b/d</i>	<i>24,15,000</i>
<i>By Subsidies</i>	<i>1,39,300</i>
<i>By Interest on investment</i>	<i>9,500</i>
<i>By Transfer fees</i>	<i>1,000</i>
<i>By Profit on sale of machinery (W.D.V. Rs.30,000)</i>	<i>25,000</i>
	<u><u><i>29,33,000</i></u></u>

Additional information :

- *Original cost of the machinery sold was Rs.40,000.*
- *Depreciation on fixed assets as per Schedule XIV of the Companies Act, 1956 was Rs. 3,42,000.*

You are required to calculate managerial remuneration in the following situations:

- (i) *when there is only whole-time director;*
- (ii) *when there are two whole-time directors; and*
- (iii) *when there are two whole-time directors, a managing director and a part-time director.* (6 marks)
- (c) *Differentiate between 'shares' and 'debentures'.* (3 marks)

Answer 3(a)

Calculation of Average Capital Employed

		<i>Rs.</i>
Fixed Assets		4,50,000
Current Assets Rs.(5,20,000 – 10,000)		5,10,000
	<i>Rs.</i>	<u>9,60,000</u>
Less : Bank overdraft	10,000	
Creditors	60,000	
Provision for taxation	<u>1,10,000</u>	1,80,000
Capital employed		7,80,000
Less : Half of the profit after tax of the current year		1,09,200
Average capital employed		<u>6,70,800</u>

Calculation of Average Adjusted Profits

Total profits for last 3 years	9,70,000
Less : Provision for bad debts	10,000
	<u>9,60,000</u>
Average Profit	3,20,000
Less : Depreciation on revaluation of fixed assets 10%	
Rs. (4,50,000 – 3,70,000)	(8,000)
	<u>3,12,000</u>
Less : Income Tax @ 30%	(93,600)
Average maintainable profit	2,18,400
Less : Normal Profit 10% of 6,70,800	(67,080)
Super Profit	<u>1,51,320</u>

Goodwill at 3 years purchase = Super profit x No. of years

$$= \text{Rs. } 1,51,320 \times 3 = \text{Rs. } 4,53,960$$

Capitalized value = (Average maintainable profit x 100) / Normal rate of profit

$$= \text{Rs. } (2,18,400 \times 100) / 10$$

$$= \text{Rs. } 21,84,000$$

$$\text{Goodwill} = \text{Rs. } 21,84,000 - \text{Rs. } 7,80,000 = \text{Rs. } 14,04,000$$

Answer 3(b)

	Rs.	Rs.
Gross profit as per Profit & Loss Account		24,15,000
<i>Add :</i> Subsidies	1,39,300	
Interest on investments	9,500	
Transfer fees	1,000	
Profit on sale of machinery (Cost – W.D.V.) (40,000 – 30,000)	10,000	1,59,800
		25,74,800
<i>Less :</i> Office and administrative expenses	3,10,000	
Director's fees	39,500	
Selling and distribution expenses	1,92,000	
Interest on debentures	18,500	
Compensation for breach of contract	27,000	
Depreciation as per Schedule XIV	3,42,000	9,29,000
		16,45,800

Computation of managerial remuneration :

- | | | |
|-------|---|--------------|
| (i) | When there is only one whole-time director : | |
| | 5% of Rs.16,45,800 | Rs. 82,290 |
| (ii) | When there are two whole-time directors : | |
| | 10% of Rs.16,45,800 | Rs. 1,64,580 |
| (iii) | When there are two whole-time directors, a
managing director and a part-time director: | |
| | 11% of Rs.16,45,800 | Rs. 1,81,038 |

Answer 3(c)

The following are the points of difference between shares and debentures :

- (i) A person holding the shares is the part-owner of the company but a person holding the debentures is the creditor of the company.
- (ii) Voting and other rights are available to shareholders and not to debenture- holders.
- (iii) Dividend is paid on shares but on debentures, interest is paid.
- (iv) A debenture holder is certain of return on his investment while a shareholder

cannot get dividend if the company does not earn profits, even if there are profits, the company does not declare a dividend.

- (v) No security is provided for shares but debentures may be secured.
- (vi) In the case of winding-up of a company, the amount of debentures will be repaid before any amount is paid to shareholders to return share capital.
- (vii) For issue of shares at a discount, certain conditions as specified in Section 79 of the Companies Act are to be satisfied but there is no restriction for issue of debentures at a discount.
- (viii) Debentures can be converted into shares but shares cannot be converted into debentures.

Question 4

- (a) Jolly Ltd. has the following balance sheet as on 31st March, 2008 :

<i>Liabilities</i>	<i>Rs.</i>
<i>Share capital :</i>	
<i>Issued, subscribed and fully paid-up (10,000 equity shares of Rs. 100 each)</i>	<i>10,00,000</i>
<i>5,000 Preference shares of Rs. 100 each</i>	<i>5,00,000</i>
<i>Capital reserve</i>	<i>1,00,000</i>
<i>Securities premium account</i>	<i>1,00,000</i>
<i>General reserve</i>	<i>2,00,000</i>
<i>Profit and loss account</i>	<i>1,00,000</i>
<i>Current liabilities</i>	<i>10,00,000</i>
	<u><u>30,00,000</u></u>
<i>Assets</i>	
<i>Fixed assets</i>	<i>22,00,000</i>
<i>Current assets</i>	<i>8,00,000</i>
	<u><u>30,00,000</u></u>

The preference shares are to be redeemed at 10% premium. Fresh issue of equity shares is to be made to the extent it is required under the Companies Act, 1956 for the purpose of this redemption. The shortfall in funds for the purpose of the redemption after utilising the proceeds of the fresh issue are to be met by taking a bank loan. Show journal entries. (6 marks)

- (b) Silver Ore Co. Ltd. was formed on 1st April, 2007 with an authorised capital of

Rs.6,00,000 in shares of Rs.10 each. Of these, 52,000 shares had been issued and subscribed but there were calls-in-arrears on 100 shares. From the following trial balance as on 31st March, 2008, prepare the trading and profit and loss account and the balance sheet :

	<i>Rs.</i>	<i>Rs.</i>
<i>Cash at bank</i>	<i>1,05,500</i>	<i>—</i>
<i>Share capital</i>	<i>—</i>	<i>5,19,750</i>
<i>Plant</i>	<i>40,000</i>	<i>—</i>
<i>Sale of silver</i>	<i>—</i>	<i>1,79,500</i>
<i>Mines</i>	<i>2,20,000</i>	<i>—</i>
<i>Promotional expenses</i>	<i>6,000</i>	<i>—</i>
<i>Interest on fixed deposit upto 31st December</i>	<i>—</i>	<i>3,900</i>
<i>Dividend on investment less 22% tax</i>	<i>—</i>	<i>3,200</i>
<i>Royalties paid</i>	<i>10,000</i>	<i>—</i>
<i>Railway track and wagons</i>	<i>17,000</i>	<i>—</i>
<i>Wages of miners</i>	<i>74,220</i>	<i>—</i>
<i>Advertising</i>	<i>5,000</i>	<i>—</i>
<i>Carriage on plant</i>	<i>1,800</i>	<i>—</i>
<i>Furniture and buildings</i>	<i>20,900</i>	<i>—</i>
<i>Administrative expenses</i>	<i>28,000</i>	<i>—</i>
<i>Repairs</i>	<i>900</i>	<i>—</i>
<i>Coal and oil</i>	<i>6,500</i>	<i>—</i>
<i>Cash</i>	<i>530</i>	<i>—</i>
<i>Investments in shares of Tin Mines</i>	<i>80,000</i>	<i>—</i>
<i>Brokerage on Tin Mines</i>	<i>1,000</i>	<i>—</i>
<i>6% Fixed deposit in Syndicate Bank</i>	<i>89,000</i>	<i>—</i>
	<u><i>7,06,350</i></u>	<u><i>7,06,350</i></u>

Depreciate plant and railway track and wagons by 10%, furniture and building by 5%. Write off one-third of the promotional expenses. Value of silver on 31st March, 2008 was Rs. 15,000. On 10th December, 2007, the directors forfeited 100 shares of which only Rs.7.50 per share had been paid. Ignore corporate dividend tax.

(9 marks)

Answer 4(a)**Journal Entries in the Books of Jolly Ltd.**

<i>Particulars</i>	<i>Dr. (Rs.)</i>	<i>Cr. (Rs.)</i>
Securities Premium A/c	Dr. 50,000	
To Premium on Redemption of Preference Shares Account		50,000
(Utilization of securities premium on Redemption of Preference Shares)		
General Reserve	Dr. 2,00,000	
Profit & Loss Account	Dr. 1,00,000	
To Capital Redemption Reserve A/c		3,00,000
(Creation of Capital Redemption Reserve to the maximum possible extent)		
Bank	Dr. 2,00,000	
To Equity Share Application and Allotment A/c		2,00,000
(Receipt of money for equity shares of Rs.2,00,000)		
Equity Share Application and Allotment Account	Dr. 2,00,000	
To Equity Share Capital Account		2,00,000
(Allotment of equity shares of the face value of Rs. 2,00,000 at par)		
Preference Share Capital Account	Dr. 5,00,000	
Premium on Redemption of Preference Shares A/c	Dr. 50,000	
To Sundry Preference Shareholders A/c		5,50,000
(Amount payable to sundry preference shareholders to redeem 5,000 preference shares of Rs.100 each at a premium of Rs.10 per share)		
Bank	Dr. 3,50,000	
To Bank Loan Account		3,50,000
(Raising a bank loan to pay off the amount due to sundry preference shareholders)		
Sundry Preference Shareholders Account	Dr. 5,50,000	
To Bank		5,50,000
(Payment made to sundry preference shareholders)		

Answer 4(b)

Silver Ore Ltd.
Trading and Profit & Loss A/c
(For the year ending March 31, 2008)

<i>Particulars</i>	<i>Rs.</i>	<i>Particulars</i>	<i>Rs.</i>
To Royalties	10,000	By Sales	1,79,500
To Wages of Mines	74,220	By Stock of Silver	15,000
To Coal and Oil	6,500		
To Depreciation on Plant	4,180*		
To Depreciation on Railway Track and Wagons	1,700		
To Gross Profit	97,900		
	<u>1,94,500</u>		<u>1,94,500</u>
To Administrative Expenses	28,000	By Gross Profit	97,900
To Promotion Expenses	2,000	By Interest on F.D. 3,900	
To Advertising	5,000	Add : Accrued 1,440	5,340
To Depreciation on Furniture and Building	1,045		
To Repairs	900	By Dividend on Investments (Grossed = 100/78 x 3,200)	4,103
To Net Profit carried to Balance Sheet	70,398		
	<u>1,07,343</u>		<u>1,07,343</u>

*NOTE : *Carriage on plant has been added to the cost of plant and depreciation is charged accordingly.*

Balance Sheet of Silver Ore Ltd.
(As on March 31, 2008)

<i>Liabilities</i>	<i>Rs.</i>	<i>Assets</i>	<i>Rs.</i>
<i>Share Capital :</i>		<i>Fixed Assets :</i>	
Authorised Capital		Mines	2,20,000
60,000 shares of Rs.10 each	6,00,000	Railway Track and Wagons 17,000	
Issued Capital :		Less : Depreciation 1,700	15,300
52,000 Shares of Rs.10 each	5,20,000	Plant 41,800	
Subscribed Capital :		Less : Depreciation 4,180	37,620
51,900 shares of Rs.10 each		Building and Furniture 20,900	
fully paid	5,19,000	Less : Depreciation 1,045	19,855
Add : Share forfeited account (100 x 7.50)	750	<i>Investment at cost :</i>	
	<u>5,19,750</u>	Shares of Tin Mines	81,000
<i>Reserves and Surplus :</i>		<i>Current Assets :</i>	
Profit and Loss Account	70,398	Stock of Silver Ore	15,000
		Cash at Bank	1,05,500
		Cash in hand	530
		Accrued Interest	1,440

<i>Liabilities</i>	<i>Rs.</i>	<i>Assets</i>	<i>Rs.</i>	<i>Rs.</i>
		<i>Loans and Advance :</i>		
		Fixed Deposit		89,000
		Tax Deducted at Source		903
		<i>Miscellaneous Expenditure :</i>		
		Promotion Expenses		4,000
	<u>5,90,148</u>			<u>5,90,148</u>

PART B

(Answer Question No. 5 which is compulsory and any two of the rest from this part.)

Question 5

(a) *State, with reasons in brief, whether the following statements are true or false :*

- (i) *At break-even point, the company earns only marginal profit.*
- (ii) *Fixed cost per unit remains fixed.*
- (iii) *Liquidity ratios measure long-term solvency of a concern.*
- (iv) *Rent on owned building is included in cost accounts.*
- (v) *Job costing can be used in industries using standard costing.*

(2 marks each)

(b) *Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :*

- (i) *Inflated price method of valuing material issue is suited when _____.*
- (ii) *Abnormal wastage _____ part of cost of production.*
- (iii) *_____ in a contract provides that the contract price would be suitably enhanced on the happening of a specified contingency.*
- (iv) *Direct material + direct labour + factory overheads = _____.*

(1 mark each)

(c) *Distinguish between any two of the following :*

- (i) *'Bin card' and 'stores ledger'.*
- (ii) *'Fixed cost' and 'variable cost'.*
- (iii) *'Absorption costing' and 'marginal costing'.*

(3 marks each)

Answer 5(a)(i)

False.

Break-even point is a point of no profit and no loss, i.e. it is the quantity or amount of sales where there is neither profit nor loss. At this point, contribution will be equal to fixed cost.

Answer 5(a)(ii)

False.

It is the total fixed cost which remains fixed irrespective of the level of output. But

the fixed cost per unit will be different at different level of output. As level of output increases the fixed cost per unit will decrease and *vice-versa*.

Answer 5(a)(iii)

False.

Liquidity ratios measure the short term solvency of a concern. These ratios indicate the relationship between current assets/liquid assets and the current liabilities of the concern.

Answer 5(a)(iv)

True.

Rent on owned building is included in cost accounts, it is done to calculate the real cost after taking into account the notional rent which would have been paid, had the building been taken on rent.

Answer 5(a)(v)

True.

Job costing can be used in industries using standard costing, since standard costing is a technique which can be used with any methods of costing including job costing.

Answer 5(b)

- (i) Inflated price method of valuing material issue is suited when there **is unavoidable wastage of material**.
- (ii) Abnormal wastage **is not** part of cost of production.
- (iii) **Escalation clause** in a contract provides that the contract price would be suitably enhanced on the happening of a specified contingency.
- (iv) Direct material + Direct Labour + Factory overheads = **Factory Cost /Works Cost**.

Answer 5(c)(i)

Bin Card and Stores Ledger

Following are the distinction between bin card and stores ledger :

<i>Bin Card</i>	<i>Stores Ledger</i>
1. It is a record of quantity	It is a record of quantity and value.
2. It is kept inside the stores.	It is kept outside the stores.
3. It is maintained by the store keeper.	It is maintained by the accounts department.
4. The postings are done before the transactions take place.	The postings are done after the transactions take place.
5. Each transaction is individually posted.	Transactions may be posted periodically and in total.

Answer 5(c)(ii)

Following are the points of distinction between fixed cost and variable cost :

1. Fixed cost is the cost which does not vary but remains constant within a given period of time and range of activity in spite of the fluctuations in production. Variable cost is the cost which varies directly in proportion to every increase or decrease in the volume of output of production. Fixed costs are sometimes referred to as “period costs” while variable costs as “product costs” in system of direct costing.
2. The variable cost per unit output remains the same while fixed cost per unit changes as the output increases or decreases and fixed cost remains constant in total.

Answer 5(c)(iii)

Following are the main distinctions between absorption costing and marginal costing:

<i>Absorption costing</i>	<i>Marginal costing</i>
(i) Fixed production overheads are charged to the product to be subsequently released as a part of goods sold i.e., it is included in cost per unit.	Fixed production costs are regarded as period cost and are charged to revenue along with the selling and administration expenses, i.e., they are not included while computing cost per unit.
(ii) Profit is the difference between sales and cost of goods sold.	Profit in marginal costing is ascertained by establishing the total contribution and then deducting there from the total fixed expenses. Contribution is the excess of sales over variable cost.
(iii) Costs are seldom classified into variable and fixed. Although such a classification is possible, it fails to establish a cost-volume profit relationship.	Cost-volume profit relationship is an integral part of marginal costing. Costs have to be classified into fixed costs and variable costs.
(iv) If inventories increase during a period, this method will reveal more profit than marginal costing. When inventories decrease, less profit are reported because under this method closing stock is valued at higher figures. Since inventories are valued at total cost, a portion of fixed overheads are also included in inventories.	If inventories increase during a period, this method generally reports less income than absorption costing; but when inventories decrease this method reports more net income. The difference in the net income is due to difference in accounting for fixed manufacturing costs as compared to inventory valuation.

<i>Absorption costing</i>	<i>Marginal costing</i>
(v) Arbitrary apportionment of fixed costs may result in under or over recovery of overheads.	Since fixed costs are excluded, there is no question of arbitrary apportionment of fixed overheads and thus no under or over absorption of overheads.

Question 6

(a) A company has provided you the following details :

<i>Liabilities</i>	<i>31.12.2007 (Rs.)</i>	<i>31.12.2008 (Rs.)</i>
<i>Share capital</i>	<i>70,000</i>	<i>74,000</i>
<i>Debentures</i>	<i>12,000</i>	<i>6,000</i>
<i>Reserve for doubtful debts</i>	<i>700</i>	<i>800</i>
<i>Trade creditors</i>	<i>10,360</i>	<i>11,840</i>
<i>Profit and loss a/c</i>	<i>10,040</i>	<i>10,560</i>
	<u><i>1,03,100</i></u>	<u><i>1,03,200</i></u>
 <i>Assets</i>		
 <i>Cash</i>	 <i>9,000</i>	 <i>7,800</i>
<i>Debtors</i>	<i>14,900</i>	<i>17,700</i>
<i>Stock</i>	<i>49,200</i>	<i>42,700</i>
<i>Land</i>	<i>20,000</i>	<i>30,000</i>
<i>Goodwill</i>	<i>10,000</i>	<i>5,000</i>
	<u><i>1,03,100</i></u>	<u><i>1,03,200</i></u>

Additional information —

— *Dividend paid Rs.3,500; and*

— *Land was purchased for Rs.10,000.*

Prepare a cash flow statement as per Accounting Standard-3 (Revised).

(6 marks)

(b) Lookahead Ltd. produces and sells a single product. Sales budget for the calendar year 2009 for each quarter is as under :

<i>Quarter</i>	<i>No. of Units to be Sold</i>
<i>I</i>	<i>12,000</i>
<i>II</i>	<i>15,000</i>
<i>III</i>	<i>16,500</i>
<i>IV</i>	<i>18,000</i>

The year 2009 is expected to open with an inventory of 4,000 units of finished product and close with an inventory of 6,500 units.

Production is customarily scheduled to provide for two-thirds of the current quarter's demand plus one-third of the following quarter's demand. Thus production anticipates sales volume by about one month. The standard cost details for one unit of the product is as follows :

- *Direct materials 10 Kgs. @ 50 paise per kg.*
- *Direct labour 1 hour 30 minutes @ Rs.4 per hour.*
- *Variable overheads 1 hour 30 minutes @ Re.1 per hour.*
- *Fixed overheads 1 hour 30 minutes @ Rs.2 per hour based on a budgeted production volume of 90,000 direct labour hours for the year.*

Answer the following —

- (i) Prepare a production budget for the year 2009 by quarters, showing the number of units to be produced. (3 marks)*
- (ii) If the budgeted selling price per unit is Rs.17, what would be the budgeted profit for the year as a whole ? (3 marks)*
- (iii) In which quarter of the year the company is expected to break-even ? (3 marks)*

Answer 6(a)

**Cash Flow Statement of
for the year ended 31st December, 2008**

	<i>Rs.</i>	<i>Rs.</i>
(A) Cash Flow from Operating Activities :		
Increase in balance of Profit & Loss A/c	520	
Adjustments for non-cash and non-operating items :		
Reserve for doubtful debts	100	
Dividend	3,500	
Goodwill written off	5,000	
Operating profits before working capital changes	9,120	
Adjustments for changes in current assets and liabilities :		
Increase in trade creditors	1,480	
Increase in debtors	(2,800)	
Decrease in stock	6,500	
Cash generated from operations	14,300	
Income-tax paid	—	
Net cash from operating activities		14,300

	<i>Rs.</i>	<i>Rs.</i>
(B) Cash Flow from Investing Activities :		
Purchase of Land	(10,000)	
Net cash used in investing activities		(10,000)
(C) Cash Flow from Financing Activities :		
Proceeds from issue of share capital	4,000	
Redemption of Debentures	(6,000)	
Dividend paid	(3,500)	
Net cash used in financing activities		<u>(5,500)</u>
Net decrease in cash and cash equivalents		
[(A) + (B) + (C)]		(1,200)
Cash and cash equivalents at the beginning of the period		<u>9,000</u>
Cash and cash equivalents at the end of the period		<u>7,800</u>

Answer 6(b)

Number of units to be sold during the year 2009

Quarter I	12,000 units
Quarter II	15,000 units
Quarter III	16,500 units
Quarter IV	18,000 units
Sales during the year	<u>61,500 units</u>

(i) Production Budget (for the year 2009 by quarters)

	<i>Quarter I Units</i>	<i>Quarter II Units</i>	<i>Quarter III Units</i>	<i>Quarter IV Units</i>	<i>Total Units</i>
Units to be produced in each quarter : 2/3rd of the current quarter's sales demand	8,000 (2/3 x 12,000)	10,000 (2/3 x 15,000)	11,000 (2/3 x 16,500)	12,000 (2/3 x 18,000)	41,000
Add: 1/3 of the following quarter's sales demand in first 3 quarters and closing inventory in the 4th quarter	5,000 (1/3 x 15,000)	5,500 (1/3 x 16,500)	6,000 (1/3 x 18,000)	6,500	23,000
Total	13,000	15,500	17,000	18,500	64,000

(1) Variable Cost per unit

		Rs.	Rs.
Direct Material	: 10 kgs. @ 50 paise per kg.	5.00	
Direct labour	: 1-½ hours @ Rs.4 per hour	6.00	
Variable overheads	: 1-½ hours @ Re.1 per hour	<u>1.50</u>	12.50

(2) Fixed overhead per annum : 90,000 hrs. @ Rs. 2 = Rs.1,80,000

(ii) Statement of Budgeted Profit for the year (as a whole)

	Rs.
Total Sales : 61,500 units @ Rs.17 per unit	10,45,000
Less : Total Variable Cost : 61,500 units @ 12.50 per unit	<u>7,68,750</u>
Contribution	2,76,750
Less : Fixed cost for the year	<u>1,80,000</u>
Profit for the year 2009 as a whole	<u>96,750</u>

(iii) Calculation of Break-even point/sales

$$\begin{aligned} \text{Break Even Point} &= \frac{\text{Fixed Overheads}}{\text{Selling Price per unit} - \text{Variable Cost per unit}} \\ &= \frac{\text{Rs. 1,80,000}}{(\text{Rs. 17} - \text{Rs. 12.50})} = 40,000 \text{ units.} \end{aligned}$$

Total sales (in units) by the end of 3rd quarter will be 43,500 (i.e. 12,000 + 15,000 + 16,500).

Therefore, the company will break-even in the later part of the 3rd quarter.

Question 7

(a) Material-A is used as follows :

- Minimum usage – 500 units per week
- Maximum usage – 1,500 units per week
- Normal usage – 1,000 units per week
- Ordering quantities – 1,600 units
- Delivery period – 4-6 weeks
- Calculate —

- (i) Maximum level. (2 marks)
- (ii) Minimum level. (2 marks)
- (iii) Ordering level. (2 marks)

- (b) On 1st July, 2007, Delux Ltd. undertook a contract for Rs.5,00,000. On 30th June, 2008 when the accounts were closed, the following details about the contract were gathered :

	Rs.
Material purchased	1,00,000
Wages paid	45,000
General expenses	10,000
Plant purchased	50,000
Materials on hand (30.6.2007)	25,000
Wages accrued (30.6.2008)	5,000
Work certified	2,00,000
Cash received	1,50,000
Work uncertified	15,000
Depreciation of plant	5,000

The above contract has an escalation clause which reads as follows :

"In the event of prices of materials and rates of wages increase by more than 5%, the contract price would be increased accordingly by 25% of the rise in the cost of materials and wages beyond 5% in each case."

It was found that since the date of signing the agreement, the prices of materials and wage rates increased by 25%. The value of the work certified does not take into account the effect of the above clause.

Prepare the contract account. (6 marks)

- (c) Differentiate between 'Halsey wage plan' and 'Rowan wage plan'. (3 marks)

Answer 7(a)

$$\begin{aligned}
 \text{Ordering level} &= \text{Maximum usage} \times \text{Maximum delivery period} \\
 &= 1,500 \times 6 = 9,000 \text{ units} \\
 \text{Minimum level} &= \text{Ordering level} - (\text{Normal usage} \times \text{Normal delivery period}) \\
 &= 9,000 - (1,000 \times 5) \\
 &= 9,000 - 5,000 = 4,000 \text{ units} \\
 \text{Minimum level} &= (\text{Ordering level} + \text{Ordering Quantity}) - (\text{Minimum usage} \times \text{Minimum delivery period}) \\
 &= (9,000 + 1,600) - (500 \times 4) \\
 &= 10,600 - 2,000 = 8,600 \text{ units}
 \end{aligned}$$

Answer 7(b)**Contract Account***Dr.**For the year ending 30th June, 2008**Cr.*

<i>Particulars</i>	<i>Rs.</i>	<i>Particulars</i>	<i>Rs.</i>
To Materials	1,00,000	By Work-in-Progress :	
To Wages (Rs.45,000 + Rs.5,000)	50,000	Work certified	2,00,000
To General Expenses	10,000	Work uncertified	15,000
To Depreciation of Plant	5,000	By Materials on hand	25,000
To Notional Profit c/d	80,000	By Contract Escalation(1)	5,000
	<u>2,45,000</u>		<u>2,45,000</u>
To Profit and Loss A/c		By Notional Profit b/d	80,000
$\left[\text{Rs. } 80,000 \times \frac{1}{3} \times \frac{\text{Rs. } 1,50,000}{\text{Rs. } 2,00,000} \right]$	20,000		
To Work-in-Progress A/c(Reserve)	60,000		
	<u>80,000</u>		<u>80,000</u>

Working Note (1)

<i>Particulars</i>	<i>Total increase Rs.</i>	<i>Upto 5% Rs.</i>	<i>Beyond 5% Rs.</i>
Materials			
$(\text{Rs. } 1,00,000 - \text{Rs. } 25,000) \times \frac{25}{125}$			
[in the ratio of 5:20]	15,000	3,000	12,000
Wages $\text{Rs. } 50,000 \times \frac{25}{125}$	10,000	2,000	8,000
Total Increase	<u>25,000</u>	<u>5,000</u>	<u>20,000</u>

Increase in contract price = 25% of increase in material and wages beyond 5%

$$= \frac{25}{100} \times \text{Rs. } 20,000 = \text{Rs. } 5,000$$

Answer 7(c)

Total wages under Halsey Wage Plan and Rowan Wage Plan is calculated as under:

*Halsey Plan :*Total Wages = Time taken x Hourly rate + $\frac{1}{2}$ (Time saved) x Hourly rate

Rowan Plan

$$\text{Total Wages} = \text{Time taken} \times \text{Hourly rate} + \left[\frac{\text{Time saved}}{\text{Standard time}} \right] \times \text{Time taken} \times \text{Hourly Rate}$$

The following are the points distinction between Halsey wage plan and Rowan wage plan:

- (i) In Halsey wage plan bonus is usually set at 50% of the time saved and it does not serve as strong incentive, whereas under Rowan wage plan bonus is that portion of the wages of the time taken which time saved bears to the standard time, and serves as a strong incentive for increasing efficiency.
- (ii) In Rowan wage plan the quality of work does not suffer much as the worker is not induced to rush through the work since bonus increases at a decreasing rate at higher levels of efficiency. In Halsey wage plan, the worker is induced to rush through the work since he gets extra wages for every 50% of the time saved.
- (iii) The effective labour rate per hour in Rowan wage plan is higher up to 50% of the time saved and falls thereafter whereas in the Halsey wage plan the effective labour rate per hour is lower up to 50% of the time saved.
- (iv) If the time taken is more than the time saved, then worker is benefitted under Rowan Plan, while in case time saved is more, workers are benefitted under Halsey Plan.

Question 8

From the following information, prepare the projected trading and profit and loss account for the next financial year ending 31st March, 2009 and the projected balance sheet as on that date :

<i>Gross profit ratio</i>	<i>25%</i>
<i>Net profit to equity capital</i>	<i>10%</i>
<i>Stock turnover ratio</i>	<i>5 times</i>
<i>Average debt collection period</i>	<i>2 months</i>
<i>Creditors velocity</i>	<i>3 months</i>
<i>Current ratio</i>	<i>2</i>
<i>Proprietary ratio (Fixed assets to capital employed)</i>	<i>80%</i>
<i>Capital gearing ratio (Preference shares and debentures to total long-term funds)</i>	<i>30%</i>
<i>General reserve and profit and loss to equity shareholders' fund</i>	<i>20%</i>
<i>Preference share capital to debentures</i>	<i>2</i>

Cost of sales consists of 40% for materials and balance for wages and overheads. Gross profit is Rs. 6,00,000.

(15 marks)

Answer 8**Projected Trading and Profit & Loss Account for the year ending March 31, 2009**

<i>Dr.</i>		<i>Cr.</i>	
<i>Particulars</i>	<i>Rs.</i>	<i>Particulars</i>	<i>Rs.</i>
To Material used	7,20,000	By Sales	24,00,000
To Wages and overheads	10,80,000		
To Gross profit c/d	6,00,000		
	<u>24,00,000</u>		<u>24,00,000</u>
To Expenses (Balancing figure)	4,93,600	By Gross profit b/d	6,00,000
To Net profit	1,06,400		
	<u>6,00,000</u>		<u>6,00,000</u>

Projected Balance Sheet as on March 31, 2009

<i>Liabilities</i>	<i>Rs.</i>	<i>Assets</i>	<i>Rs.</i>
Share Capital :		Fixed Assets	15,20,000
Equity Share Capital	10,64,000	Current Assets :	
Preference Share Capital	3,80,000	Stock	3,60,000
Reserves and Surplus :		Debtors	4,00,000
General Reserve	1,59,600		
Profit & Loss Account	1,06,400		
Secured Loans :			
Debentures	1,90,000		
Current Liabilities :			
Trade Creditors	1,80,000		
Bank Overdraft	2,00,000		
	<u>22,80,000</u>		<u>22,80,000</u>

Working Notes :

- Rs.
- (i) Gross Profit 6,00,000
Gross Profit being 25% of sales
Sales = Rs. 6,00,000 x 100/25 = Rs. 24,00,000
- (ii) Cost of Sales = Sales – Gross profit
= Rs. 24,00,000 – Rs. 6,00,000 = Rs. 18,00,000

- (iii) Material used = 40% of Cost of sales
 $= 40/100 \times \text{Rs. } 18,00,000 = \text{Rs. } 7,20,000$
- (iv) Wages and overheads = Rs. 18,00,000 – Rs. 7,20,000 = Rs. 10,80,000
- (v) Stock = Cost of sales / Stock turnover ratio = Rs. 18,00,000/5 = Rs. 3,60,000
- (vi) Debtors = Sales for 2 months = Rs. 24,00,000 x 2/12 = Rs. 4,00,000
- (vii) As current ratio is 2, Current liabilities are half of current assets
Hence, current liabilities = $\frac{1}{2} \times (\text{Rs. } 3,60,000 + \text{Rs. } 4,00,000) = \text{Rs. } 3,80,000$
- (viii) Trade Creditors = 3 months of material consumed
 $= \text{Rs. } 7,20,000 \times 3/12 = \text{Rs. } 1,80,000$
- (ix) Bank overdraft = Rs. 3,80,000 – 1,80,000 = Rs. 2,00,000
- (x) Fixed assets to capital employed = 80%
Hence, working capital to capital employed = 20%
Working Capital = Current assets – Current liabilities
 $= (\text{Rs. } 3,60,000 + \text{Rs. } 4,00,000) - \text{Rs. } 3,80,000 = \text{Rs. } 3,80,000$
Fixed assets = Rs. 3,80,000 x 80/20 = Rs. 15,20,000
- (xi) Total long term funds = Fixed Assets + Working Capital
 $= \text{Rs. } 15,20,000 + \text{Rs. } 3,80,000 = \text{Rs. } 19,00,000$
- (xii) Capital gearing ratio being 30% (Preference share capital plus debentures to Total Long Term Funds)
 $= 30\% \text{ of Rs. } 19,00,000 = \text{Rs. } 5,70,000$
Preference share capital = Rs. 5,70,000 x 2/3 = Rs. 3,80,000
- (xiii) Debentures = Rs. 5,70,000 x 1/3 = Rs. 1,90,000
- (xiv) Equity Shareholders' Fund = Rs. 19,00,000 – Rs. 5,70,000 = Rs. 13,30,000
General reserve and Profit & Loss Account = 20% of equity shareholders' fund
 $= 20\% \text{ of Rs. } 13,30,000 = \text{Rs. } 2,66,000$
Equity share capital = Rs. 13,30,000 – Rs. 2,66,000 = Rs. 10,64,000
- (xv) Net profit = 10% of Equity share capital = Rs. 1,06,400
- (xvi) General Reserve = Rs. 2,66,000 – Rs. 1,06,400 = Rs. 1,59,600
-